

Dependent Eligibility Audits



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In the economic downturn, employers are forced to look at every possible angle for savings. Even companies that are not suffering right now are examining all of their cost centers such as payroll, staffing, outsourcing, administrative expenses, travel expenses and the like. Employers are also reconsidering their budgets for employee benefits. They are finding ways to eliminate or reduce costs or shift them to employees in the form of increased premiums, buy-up plans or worksite benefits.

The employee benefit that seems to get the most play is health insurance. Health insurance is the biggest budgetary item for most employers, usually second only to payroll costs. The tricky thing about health insurance is that although it is the most expensive, it is also the most prized benefit among employees.

As a result, employers are very careful about making changes such as increasing employee contributions into the plan, increasing co-payments and coinsurance, all which result in significant out of pocket costs for employees. Smart employers, however, should look internally and examine how else they can make their health insurance plan run lean. A **dependent eligibility audit** is a tool that employers can use.

What is a Dependent Eligibility Audit?

A dependent eligibility audit is a process by which an employer, or a third-party vendor, reviews each dependent enrolled on the medical and dental plans and verifies their eligibility for coverage.

Independent auditors will report that the typical dependent eligibility audit will remove from 5%-12% of dependents from a health plan. If the average annual cost of a dependent is around \$3,000, this could result in plan savings of as much as 5-15%. In a self-funded medical and dental plan, where employers fund their own medical and dental claims from the assets of the company, this savings goes directly to an employer's bottom line.

By way of example, the state of New Jersey did a dependent eligibility audit in February 2009 on 224,000 state and local workers. They realized that they had as many as 10,000 to 15,000 ineligible dependents on the healthcare plan. Over the past five years, it is estimated that the state spent as much as \$185 million dollars in claims on ineligible people. Performing this kind of audit is becoming a necessity for all employers, especially the larger companies with low turnover, since employee's family situations change over time and the paperwork is not always updated.

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Why Initiate a Dependent Eligibility Audit

There are several business and ethical reasons why an employer should conduct a dependent eligibility audit. Cost-savings is the most compelling. If there are people either erroneously or fraudulently on an insurance plan, it can cost an employer thousands of unnecessary dollars in both claims and administrative expense which is unacceptable in this economic environment. Verifying each dependent's eligibility is a way to contain insurance costs without asking employees to pay more to support the plan. Additional reasons include:

- The employer has a responsibility under ERISA to ensure that plan dollars are used for the sole benefit of employees and their eligible dependents.
- The likelihood of this type of fraud is more prevalent now. Financial strain on many families and a high rate of unemployment may prompt individuals to knowingly cover ineligible dependents out of necessity and desperation.
- The employer bears a fiscal responsibility to the plan and the plan participants. If there are excess claim dollars under these plans that are being unjustly paid out, it is unfair not only to the employer but to all of the employees who support the plan financially.
- If the employer offers pre-tax health insurance premiums to employees under Section 125 of the IRC, it is problematic to extend this tax shelter for dependents that are not eligible under the plan.
- Further, all companies, whether public or private, have stakeholders. Stakeholders are those vested in a company's success. An employer has a responsibility to take an active role in this. Protecting the assets of the company is essential to this function.
- For public traded companies, Sarbanes-Oxley requirements may view coverage for ineligible dependents, whether knowingly or unknowingly, as a shortcoming of the employer that must be captured by an independent auditor and reported to stockholders.

How to Perform a Dependent Eligibility Audit

A dependent eligibility audit can be performed in several different ways. It can be done in-house or it can be outsourced to a third party vendor who specializes in audits of this nature. It can take the form of a mail campaign or a worksite arrangement where employees meet one-on-one with representatives to review the dependents covered under their name.

Although this can be a fairly sensitive topic for employees, it is best for the employer to take full ownership of the project and co-brand the audit if partnering with an outside firm. The employees need to know that responding to these inquiries is required. In most cases, employees appreciate the efforts of the employer and recognize that these steps are being taken for the overall good of the company.

At the outset of an audit, it is only fair to give the employees the benefit of the doubt. Many plans have complicated eligibility definitions and a lean Human Resources Department might be inadequate to assist employees when they first enroll. Since many of the ineligible dependents are enrolled erroneously, it is recommended that first, an **Amnesty period** be implemented for all employees. This allows employees to take a look at those enrolled on the plan and verify each dependent's eligibility. If they find someone on the plan that should not be, they can be removed, no questions asked and no recourse for benefits that have already been paid out.

A timeline of a full dependent eligibility audit might look like this:

- 1) **Initial Communication** about the dependent eligibility audit, the timeline of the project and the target date of completion.
- 2) **An Amnesty Letter** to each employee with covered dependents. This letter will outline the consequences, if the company chooses to impose any, for those who do not come forward at this time.
- 3) **A Mail or Worksite procurement** where dependent verification is collected in the form of affidavits, student verifications, court orders and the like. An appeals process should be identified to all employees as well.

Typically ineligible dependents are found in one of the following categories:

- Ex-spouses with court-ordered health coverage
- Common law spouses
- Step children, foster children, married children, grandchildren
- Students not enrolled in an accredited institution
- Students who exceed the maximum age
- Friends, roommates, other relatives
- Domestic partners (when an employer has not chosen to cover them)

There is a definite Return on Investment (ROI) for a dependent eligibility audit. Though there may be a cost to run the audit, especially if an outside firm is hired, an ROI can be calculated after the audit is complete. In many cases, an outside auditor will guarantee a certain savings that can help make the argument to proceed with an audit.

For more information on Dependent Eligibility Audits, please contact your Account Executive at William Gallagher Associates.

